

DRAFT



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	05/26/05	Bill No:	AB 1099
Tax:	Property	Author:	Leno
Related Bills:	SB 1017 (Campbell)		

BILL SUMMARY

This bill would extend the new construction exclusion for active solar energy systems to improvements constructed through the 2008-09 fiscal year.

Summary of Amendments

The amendments extend the new construction exclusion to the 2008-09 fiscal year rather than indefinitely.

ANALYSIS

Current Law

The California Constitution, Article XIII A, Section 2(c)(1), grants the Legislature the authority to exclude the construction or addition of any active solar energy system from the definition of assessable new construction.

Section 73 of the Revenue and Taxation Code is the implementing statute for this new construction exclusion. Its provisions are scheduled to sunset on January 1, 2006.

Proposed Law

This bill would extend the new construction exclusion to the 2008-09 fiscal year and provides for an automatic repeal of its provisions on January 1, 2010.

In General

Property Tax System. Article XIII, Section 1 of the California Constitution provides that all property is taxable, at the same percentage of “fair market value,” unless specifically exempted, or authorized for exemption, within the Constitution. Article XIII A, Section 2 of the California Constitution defines “fair market value” as the assessor’s opinion of value for the 1975-76 tax bill, or, thereafter, the appraised value of property when purchased, newly constructed, or a change in ownership has occurred. This value is generally referred to as the “base year value.” Barring actual physical new construction or a change in ownership, annual adjustments to the base year value are limited to 2% or the rate of inflation, whichever is less. Article XIII A, Section 2 provides for certain exclusions from the meaning of “change in ownership” and “newly constructed” as approved by voters via constitutional amendments.

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New Construction. The constitution does not define the term “new construction.” Revenue and Taxation Section 70 defines it, in part, to mean:

Any addition to real property, whether land or improvements (including fixtures), since the last lien date.

Any alteration of land or improvements (including fixtures) since the lien date that constitutes a “major rehabilitation” or that converts the property to a different use. A major rehabilitation is any rehabilitation, renovation, or modernization that converts an improvement or fixture to the substantial equivalent of a new improvement or fixture.

With respect to any new construction, the law requires the assessor to determine the added value upon completion. The value is established as the base year value for those specific improvements qualifying as “new construction” and is added to the property’s existing base year value. When new construction replaces certain types of existing improvements, the value attributable to those preexisting improvements is deducted from the property’s existing base year value. (R&T Code §71)

New Construction Exclusions. Certain types of construction activity is excluded from assessment as “new construction” via constitutional amendment. Consequently, while these improvements may increase the value of the property, the additional value is not assessable.

Prop	Election	Subject	Code
8	November 1978	Disaster Reconstruction	§70(c)
7	November 1980	Active Solar Energy Systems	§73
23	June 1984	Seismic Safety (Unreinforced Masonry)	§70(d)
31	November 1984	Fire Safety Systems	§74
110	June 1990	Disabled Access Improvements (Homes)	§74.3
127	November 1990	Seismic Safety Retrofitting & Hazard Mitigation	§74.5
177	June 1994	Disabled Access Improvements (All Properties)	§74.6
1	November 1998	Environmental Contamination Reconstruction	§74.7

Overview of Solar Energy New Construction Exclusion

An “active solar energy system” is defined in Section 73 as a system that uses solar devices, which are thermally isolated from living space or any other area where the energy is used, to provide for the collection, storage, or distribution of solar energy. Such a system does not include solar swimming pool heaters, hot tub heaters, passive energy systems, or wind energy systems.

An active solar energy system may be used for any of the following:

- Domestic, recreational, therapeutic, or service water heating.
- Space conditioning.
- Production of electricity.
- Process heat.
- Solar mechanical energy.

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An active solar energy system includes storage devices, power conditioning equipment, transfer equipment, and parts related to the functioning of those items. "Parts" includes spare parts that are owned by the owner of, or maintenance contractor for, an active solar energy system for which the parts were specifically purchased, designed, or fabricated for installation in that system. Such a system includes only equipment used up to, but not including, the stage of transmission or use of the electricity.

An active solar energy system also includes pipes and ducts that are used *exclusively* to carry energy derived from solar energy. Pipes and ducts that are used to carry *both* energy derived from solar energy and energy derived from other sources may be considered active solar energy system property only to the extent of 75 percent of their full cash value.

An active solar energy system does not include auxiliary equipment, such as furnaces and hot water heaters, that use a source of power *other* than solar energy to provide usable energy. Dual use equipment, such as ducts and hot water tanks, that is used by both auxiliary equipment and solar energy equipment is considered active solar energy system property only to the extent of 75 percent of its full cash value.

Legislative History of Solar Energy New Construction Exclusion

Proposition 7 (SCA 28, Alquist) was approved by voters in 1980 and amended the California Constitution by giving the Legislature the authority to exclude from property tax assessment the construction of active solar energy systems.

SB 1306 (Stats. 1980, Ch. 1245; Alquist) added Section 73 to the Revenue and Taxation Code to implement Proposition 7. Its provisions were operative for five fiscal years - 1981-82 through 1985-86.

AB 1412 (Stats. 1985, Ch. 878; Wyman), extended the exclusion for another five fiscal years - 1986-87 through 1990-91. It also required the Legislative Analysts Office to report to the Legislature by January 1, 1990 on the fiscal and economic effects of the exclusion.

SB 1311 (Greene) in 1989 proposed repealing the exclusion on January 1, 1990. SB 1311 was not heard in any committee.

AB 4090 (Wyman, Alquist) in 1990 proposed extending the exclusion through the 1993-94 fiscal year. AB 4090 passed both houses, but was vetoed by the Governor Deukmejian. The Governor's veto messages stated that he supported efforts to encourage the development of solar energy in California, but the bill would have resulted in millions of dollars of property tax revenue loss to local entities in the high desert region of the state and solar energy income tax credits were otherwise available. At that time, a major commercial project to build solar-electrical generating facilities (SEGS) in the Mojave Desert near Barstow in San Bernardino County was underway by Luz International Ltd.

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SB 103 (Stats. 1991, Ch. 28; Morgan) extended the exclusion for three more fiscal years - 1991-92 through 1993-94. SB 103 added a new Section 73 to the code, since the prior Section 73 was repealed by its own provisions on January 1, 1991. However, SB 103 was urgency legislation effective May 14, 1991 and drafted so the continuity of the exclusion would not be affected. SB 103 included a provision to automatically repeal its provisions on January 1, 1995 absent future legislative action. No legislation was enacted prior to the repeal date so the exclusion was not available for five fiscal years (1994-95 through 1998-99) until AB 1755 was enacted as noted below.

SB 1553 (Alquist) in 1994 would have, in part, extended the exclusion indefinitely, however these provisions were amended out of this bill prior to its enactment.

AB 1755 (Stats. 1998, Ch. 855; Keeley) re-established the exclusion for six fiscal years - 1999-2000 through 2004-05. The current exclusion will end on June 30, 2005 and Section 73 will be automatically repealed by its own provisions on January 1, 2006.

SB 116 (Peace) in 1998 would have, in part, also re-established the exclusion. This bill was not enacted.

COMMENTS

1. **Sponsor and Purpose.** The California Solar Energy Industries Association is sponsoring this bill to insure that persons who will be installing active solar energy systems will not incur additional property taxes due to those improvements.
2. **The May 26, 2005 amendments** extend the new construction exclusion to the 2008-09 fiscal year instead of indefinitely.
3. **Except for a five-year hiatus for fiscal years 1994-95 through 1998-99 the exclusion has been available since 1981.** This bill would ensure the continuity of the exclusion.
4. **Suggested Amendment.** Existing law, subdivisions (d) and (e) of Section 73, are internally inconsistent and create a six-month limbo period in the last fiscal year that the provision is operative (i.e., June 30, 2005 to January 1, 2006). Specifically, subdivision (d) implies that the new construction exclusion is unavailable after June 30, 2005 (the last date of the 2004-05 fiscal year), but subdivision (e) states the provisions of the section are "in effect" until January 1, 2006. This bill would inadvertently perpetuate this six-month limbo period in the last fiscal year (2008-09) the provisions are available (i.e., June 30, 2009 to January 1, 2010). Because of the creation of supplemental assessments, a reference to the "lien date" in conjunction with the fiscal year has been generally rendered obsolete when the provision relates to a change in ownership or new construction issue. Consequently, the following technical amendment is suggested:

(d) This section applies to ~~property tax lien dates for the 1999-2000 fiscal year and for each fiscal year thereafter to the 2008-09 fiscal year, inclusive. For purposes of supplemental assessment, this section applies only to qualifying construction or additions completed on or after January 1, 1999.~~

(e) This section shall remain ~~in effect~~ operative only until January 1, 2010, and as of that date is repealed.

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5. **Related Bill.** Senate Bill 1017 (Campbell) would also extend the new construction exclusion to the 2016-2017 fiscal years. However, this bill has yet to be heard in a committee.

COST ESTIMATE

The Board would incur some minor absorbable costs in informing and advising county assessors, public and staff of the law changes.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

AB 1755, Chapter 855, Statutes of 1998, reinstated new construction exclusion for active solar energy systems. Since 1998, the number of active solar energy systems, primarily known as grid-connected photovoltaic (PV), installations located at residential and commercial customer sites has increased by an average of more than 2,000 units each year. The increase is due in large part to federal and state programs that offer tax credits and other cost cutting measures such as the California Energy Commission's Renewable Energy Rebate and Buydown Program, and attractive commercial and residential financing options. In 1998, PV generated electricity was more expensive than conventional utility-supplied electricity when amortized over the life of the system. However, since then, the increase in the cost of utility-supplied electricity and attractive rebate and buydown programs have made PV systems a more cost beneficial alternative, especially for new home construction. In a December 2004 article published by the Environment California, a survey of nine communities was measured; it found that homeowners can expect to save on average \$4,500 over a lifetime of 30 years on their solar investment. However, Commercial PV systems can be very costly, in a Property Tax Department phone survey of County Assessor's; one county reported a \$4 million commercial PV system was excluded from the property tax roll. In the past, customers have installed PV systems primarily for environmental commitment, and not for financial reasons. However, sentiments have changed; the question is whether sentiments have changed enough to prompt an appraiser to value a house with a PV system at a greater value than another house identical in value with all other amenities, including location, being equal. The construction does not necessarily enhance the value of the property and, therefore, no taxable value might be added for new construction. Even though current incentives and the increase in electric utility rates have made PV installations more attractively priced, it is debatable whether the addition of a PV system would add significantly to the value of the property. Finally, based on the result of a phone survey of County Assessor's, the revenue impact of the exclusion was found to be minimal.

Since 1999, the California Energy Commission's Renewable Energy Program, has provided funding for more than 12,000 commercial and residential PV systems at a value of \$447.4 million, an average of \$74.6 million in completed projects per year. If these solar energy systems had been included in property tax rolls, and the value of these systems were determined to have added value to the property, the property tax revenue impact would have been \$746,000 for each year (\$74.6 million x 1% basic property tax rate).

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Revenue Summary

The revenue effect from extending new construction exclusion for active solar energy systems would be minimal.

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